

Message Text

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ACTION EUR-12

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FM AMCONSUL MILAN
TO SECSTATE WASHDC 5148
INFO AMEMBASSY ROME
USMISSION OECD PARIS
USMISSION EC BRUSSELS

C O N F I D E N T I A L SECTION 1 OF 2 MILAN 2769

E.O. 11652: GDS
TAGS: ECON, EFIN, ELAB, EINV, IT
SUBJECT: AMERICAN BUSINESS IN MILAN TAKES STOCK OF ITSELF
AND ITALY

SUMMARY: AMERICAN BANKING AND INDUSTRY LEADERS IN
MILAN ARE GENERALLY MORE PLEASED WITH OWN PERFORMANCE
AND LESS FEARFUL OF FUTURE THAN NEWSPAPERS MIGHT
LEAD ONE TO THINK. THEY FEEL ITALY MUST SWALLOW
BITTER ECONOMIC MEDICINE BEING PRESCRIBED FOR HER.
PATIENT WOULD BEGIN TO FEEL REAL SHOCK IN EARLY
SPRING. IF MEDICINE ACCEPTED, HOWEVER, THEY SEE
CONDITIONS HERE AS FAVORING RETURN TO ECONOMIC
HEALTH. BUT CURE WILL REQUIRE PERIOD OF TWO TO
THREE YEARS. END SUMMARY.

2. HEADS OF AMERICAN BANKS AND BUSINESSES IN
MILAN TOLD US DURING THIRD WEEK OF DECEMBER THAT
THEY ARE GENERALLY DOING PRETTY WELL. SO WERE NUMBER
OF ITALIAN COMPANIES, ESPECIALLY SOME SMALL TO MEDIUM
SIZED ONES THAT ARE ACTUALLY HAVING TROUBLE MEETING
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FOREIGN DEMAND AND DELIVERY DATES. THEY ADDED
THAT THEY SEE PLENTY OF HOPE FOR ITALIAN
ECONOMY IF ITALY ADOPTS TOUGH AUSTERITY MEASURES
BEING URGED ON HER BY INTERNATIONAL FINANCIAL COM-
MUNITY. THEY REITERATED COMMON WISDOM THAT ITALY'S
KEY PROBLEM INVOLVES BALANCE OF PAYMENTS: COUNTRY

BUYS ABROAD MORE THAN IT SELLS. ITALY MUST THEREFORE PRODUCE MORE AND CONSUME LESS. IN THREE ROUNDTABLE DISCUSSIONS AT CONSULATE, CONTINUING SERIES BEGUN SEVERAL YEARS AGO, PARTICIPANTS TOLD US HOW THEY FELT ITALY IS COPING WITH MAJOR PROBLEMS OF INFLATION, SUPPORT FOR LIRA, INVESTMENT, AND LABOR OPPOSITION TO STRUCTURAL REFORMS. AND THEY EXPLAINED HOW THEIR OWN INTERESTS ARE BEING AFFECTED AS ITALY SEARCHES FOR SOLUTIONS.

3. ANDREOTTI AUSTERITY MEASURES, MAIN VEHICLE FOR DAMPENING DEMAND AND THEREBY CONTAINING INFLATION AND RIGHTING BALANCE OF PAYMENTS, WERE EVALUATED QUITE DIFFERENTLY BY BANKERS, ON ONE HAND, AND BUSINESS PEOPLE, ON OTHER. BANKERS POINTED TO RESILIENCY OF ITALIAN ECONOMY AND ABILITY TO MAKE QUICK TURN AROUNDS IN BALANCE OF PAYMENTS. THEY SAW PARTIAL WAGE FREEZE, GASOLINE PRICE RISE, AND OTHER MEASURES AS LIKELY TO CAUSE SUBSTANTIAL DROP IN INTERNAL DEMAND. PERHAPS TOO SUBSTANTIAL. THEY NOTED NET DROP IN ITALIAN DEMAND--AND PRODUCTION--IN OCTOBER FOR FIRST TIME IN YEAR AND SOME THOUGHT EVENTUAL FALL IN PRODUCTION AND EMPLOYMENT MIGHT BE MORE THAN COUNTRY COULD TAKE SOCIALLY AND POLITICALLY. POLITICAL AND ECONOMIC CRUNCH WOULD COME IN EARLY SPRING. EXPORTS WERE PARTIAL ANSWER AND WERE IN FACT DOING VERY WELL. SOME SECTORS BOOMING. BUT EXPORTS WERE BECOMING INCREASINGLY ANSWER FOR MORE AND MORE COUNTRIES, SITUATION THAT OBVIOUSLY COULD NOT CONTINUE INDEFINITELY. INTERNAL DEMAND HAD TO

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BE SUSTAINED AT LEAST AT MINIMUM LEVELS. BANKERS DID NOT THINK GROWTH WOULD SINK ALL THE WAY TO ZERO, AS ONE BANK OF ITALY MODEL PREDICTED, BUT THEY WERE CONCERNED NONETHELESS.

4. BUSINESS TYPES, ON OTHER HAND, WERE ONLY MILDLY WORRIED ABOUT RECESSION AND CRITICIZED AUSTERITY MEASURES AS TOO WEAK. INFLATION AND BALANCE OF PAYMENTS SITUATIONS, NOT SUPPORT FOR DOMESTIC DEMAND, WERE PLACES TO PUT EMPHASIS. EVEN WITH STRINGENT AUSTERITY MEASURES, THEY STRESSED, IT WOULD TAKE ITALY TWO OR THREE YEARS TO GET HER INTERNATIONAL ACCOUNTS BACK IN BALANCE.

5. US COMPANIES WERE GENERALLY CONFIDENT ABOUT THEIR OWN POSITIONS IN ITALIAN MARKET. US BANKS ARE MAKING MONEY, AND NEW ONE IN FACT--MANUFACTURERS HANOVER TRUST--IS STARTING OPERATIONS IN MILAN,

BRINGING TOTAL U.S. BANKS REPRESENTED HERE TO ELEVEN. (BANKS DID REPORT, SURPRISINGLY, THAT ITALIAN BUSINESS MAKES NO USE OF FORWARD EXCHANGE MARKETS.) AMERICAN MANUFACTURERS AND RETAILERS SAID PRODUCTION HAD BEEN SUBSTANTIALLY HIGHER IN 1976 THAN 1975, AND IN MANY CASES PROFITS AS WELL. IN THOSE SECTORS LIKE OIL AND PHARMACEUTICALS WHERE GOVERNMENT PRICE CEILINGS DEPRIVED FIRMS OF PROFITS, COMPANIES APPEARED CONTENT TO DIG IN AND WAIT FOR BETTER TIMES. NEVERTHELESS, THEY ARE FEELING PAIN. RESIGNATION OF ESSO PRESIDENT SALA WAS SEEN AS REACTION TO CONTINUED HEAVY LOSSES WHICH LOCAL MANAGEMENT HARD PRESSED TO JUSTIFY TO PARENT COMPANIES. ALL EXCEPT THESE LATTER THOUGHT 1977 WOULD BE FAIRLY GOOD YEAR, IF NOT AS GOOD AS THIS ONE.

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C O N F I D E N T I A L SECTION 2 OF 2 MILAN 2769

6. SHORT TERM FUTURE FOR LIRA AND STATE OF ITALIAN RESERVES ELICITED SURPRISING OPTIMISM FROM AMERICANS. BANKS THOUGHT RESERVES WOULD BE ADEQUATE TO GET ITALY THROUGH APRIL--AND MAYBE EVEN TO FALL--WITH LIRA NOT GOING MUCH BEYOND 930 TO DOLLAR (LESS THAN REAL RATE NOW, AFTER ADJUSTMENT MADE FOR EXCHANGE RESTRICTIONS). CONTRIBUTING TO GOOD RESERVE POSITION WAS VERY SATISFACTORY PROGRESS ON REPATRIATION OF CAPITAL (ESTIMATED AT OVER 1 BILLION DOLLARS, ALL IN LAST MONTH OR TWO).MOREOVER, ACCOUNTANTS AND BANKERS, KNOWLEDGEABLE ABOUT OTHER PEOPLE'S

MONEY, THOUGHT THAT DECLARATION OF FOREIGN OWNERSHIP OF ASSETS LARGELY RESPECTED AND WOULD NOT ONLY SLOW FUTURE CAPITAL EXPATRIATION BUT ALSO INCREASE TAX TAKE--A CONCLUSION SUPPORTED BY OTHER EVIDENCE WE HAVE SEEN.

7. US FIRMS ACKNOWLEDGED THAT FOREIGN INVESTMENT HERE, IN WHICH THEY ALL HAVE DIRECT INTEREST, IS STILL PROBLEM FOR ITALY. THEY CRITICIZED ON THIS SCORE MAIN AUSTERITY MEASURE--PARTIAL WAGE ESCALATION--
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FINANCIAL FREEZE AND TURNING OF MONEY SAVED INTO NON-NEGOTIABLE GOVERNMENT BONDS--AS CHEAP GOVERNMENT FINANCING AND DEPRIVATION FOR COMPANIES WHICH COULD OTHERWISE INVEST MONEY. LAWS LIKE THAT EXPLAINED WHY NO NEW FOREIGN COMPANIES WOULD BE COMING TO ITALY SOON, EVEN WHEN MANY ITALIAN FIRMS WERE ON MARKET AT BARGAIN PRICES. AT SAME TIME, US FIRMS NOT THINKING OF DISINVESTING, NOT EVEN COMPANIES WHICH GOVERNMENT PRICE-FIXING WAS KEEPING IN RED. AND ONE VERY LARGE COMPANY WAS EVEN MAKING SIZEABLE NEW INVESTMENTS TO SUPPLEMENT EXISTING ONES. CRITERIA, HOWEVER, WERE HIGH PROFIT AND QUICK, LIQUID RETURN (AMORTIZATION WITHIN THREE YEARS) WITH CONCENTRATION ON MONEY MAKING LINES.

8. AMERICAN COMPANIES THOUGHT LABOR UNION COMPORTMENT HAD TAKEN VERY DEFINITE TURN FOR BETTER. GENERAL FEELING, BASED APPARENTLY ON FIRMS' OWN IMPROVED DEALINGS WITH LABOR, WAS THAT UNIONS ARE STARTING TO ACCEPT PROFIT PRINCIPLE AND TO DRAW CONSEQUENCE THAT THEY MUST ACCEPT SOME RESPONSIBILITY FOR COMPANY WELL-BEING. THAT WAS BIG CHANGE FROM PRACTICE OF PAST YEARS AND A PROMISING FACTOR FOR ALL.

9. ALL IN ALL, AMERICAN ENTERPRISE IN ITALY SAW TOUGH SLEDDING HERE IN SHORT RUN, WITH ITSELF AFFECTED LESS HARSHLY HOWEVER THAN ITALIAN COMPANIES. (ACCESS TO NON-ITALIAN FINANCING, FOR EXAMPLE, HAS KEPT AMERICAN FIRMS OUT OF DEEP INDEBTEDNESS THAT PLAGUES ITALIAN COUNTERPARTS.) REAL AUSTERITY MEASURE HAD TO BE IMPLEMENTED AND SCREWS KEPT ON FOR SOME TIME. ONCE, HOWEVER, INFLATION IS UNDER CONTROL, BALANCE OF PAYMENTS TENDENCIES PUT IN RIGHT DIRECTION, AND BUSINESS CAN BEGIN TO CLIMB OUT FROM UNDER HEAVY DEBT LOAD,
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CONDITONS WERE HERE FOR NOTABLE GROWTH. UNION
OBDURANCE TO KEEPING COST OF LABOR AT COMPETITIVE
LEVELS WAS STARTING TO CHANGE. STEADY IMPROVEMENT
WAS EVIDENT IN TAX MORALITY BY BUSINESS AND INDIVI-
DUALS ACCOMPANIED BY SOME IMPROVEMENT IN TAX
COLLECTION ADMINISTRATION. WHEN EFFECTS OF THESE
DEEP-SEATED CHANGES STARTED TO BE FELT, FOREIGN
INVESTMENT WOULD COME BACK (REASONS FOR ITS ABSENCE
BEING MORE ECONOMIC THAN FEAR OF COMMUNISTS). SO
AMERICAN BUSINESS WAS STAYING, AND EXPECTING BETTER
TIMES.FINA

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